FLORIDA COMMERCE
CREDIT UNION
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March 8, 2010

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428

Delivered Via E-Mail: regcomments@ncua.gov

Re: Comments on Part 704 Corporate Credit Unions

Dear Ms. Rupp:

On behalf of Florida Commerce Credit Union ("Florida Commerce") representing approximately 36,200 members, we are pleased for the opportunity to provide this response on behalf of our members to the proposed amendments on Part 704 Corporate Credit Unions.

In 2010, Florida Commerce celebrates its 70th birthday and has a long history of involvement with corporate credit unions, both as a member and as a customer of many of the services offered by corporate credit unions. It is through these lenses that we provide our comments.

It appears from the proposed rule that the NCUA is moving towards eliminating wholesale corporates and replacing them with a regulatory capital structure that applies equally to all corporates. The current capital structure is being replaced with a risk-weighted, tiered system similar to those in place for banking capital regulations, tailored somewhat to reflect the corporate's role as a liquidity provider. Our comments on the rule are as follows:

## I. **Capital Requirements:**

The proposed rule re-designates existing membership capital (MCA) as the newly created term Perpetual Contributed Capital (PCC). The corporate would be required to meet new capital ratios within one year of the effective date of the rule. Our concern with this rapid timeline is that many corporates will be unable to obtain these levels, which will place them in PCA. We recommend allowing more time for the phase- in for the risk-based capital ratios and for the minimum leverage ratios.

Further, we are concerned with the elimination of the prohibition against conditioning membership on the purchase of perpetual capital. We believe this should remain in the regulation. If member paid-in-capital can be used to recover losses that exceed retained earnings, it's going to be difficult for any natural person credit unions to recapitalize the corporate. The corporate will have a difficult time creating enough value to individual member credit unions sufficient to meet the retained earnings requirements.

Finally, regarding the prohibition on paying dividends in s. 704.4 on capital accounts for a corporate deemed undercapitalized, we believe this provision should be amended to apply only to those corporate credit unions that are either significantly or critically undercapitalized.

## II. **Corporate Governance:**

The rule appears to limit the pool of persons that may serve on the board to only natural person CEO's, CFO's or COOs of natural person credit unions. we believe this may unjustifiably narrow the pool of potential board members and may eliminate the ability of a corporate to have persons who may bring special expertise that could be of value to the corporate. We would recommend language suggesting that only a majority of board members need to contain the designation of CEO, CFO or COO, but not necessarily requiring the same for all board members. We would not be opposed to language requiring minimum director experience or knowledge requirements or continuing education requirements.

The rule also imposes a limit of 6 consecutive years on the same corporate board. We would recommend at least allowing 12 years, as we believe it takes time for a board member to fully learn and understand the organization and develop the expertise to make informed decisions. The retention of institutional knowledge is also an asset that should be valued for purposes of board governance. A 6-year term limit diminishes that capability.

Finally, we believe the prohibition on indemnification of board members is not warranted. In fact, if it is the intent of the NCUA to increase the standards and qualifications of board members, this would appear to have the opposite effect. By increasing the risk of potential liability to a board member, this may in fact discourage otherwise qualified and capable persons from serving on the board. A director acting in good faith and otherwise utilizing good business judgment should enjoy this protection.

## III. Asset Liability Management

### a. Prohibition Against Redeeming Certificates at a Premium

The rule requiring corporate credit unions to charge a market-based penalty on early withdrawals sufficient to cover the replacement cost of the certificate/share redeemed should be retained. We disagree with the proposed rule limiting a corporate's ability to pay a market-based redemption price to no more than par, eliminating the ability to pay a premium on early withdrawals. We don't feel this change is warranted.

### b. Cash Flow Mismatch Sensitivity Analysis

The proposal requires that a corporate shock both its assets and liabilities by 300 bp at least quarterly and ensure that credit spread shock does not result in an NEV ratio of less than two percent (if less than three percent (3%) then monthly testing will be required) and that the NEV does not decline by more than 15 percent.

We believe that using a 300 basis point credit spread shock may be appropriate for some instruments; however, it is not appropriate for others such as GSE debentures. Additionally, the proposal would benefit from recognizing that instruments from similar issuers but with shorter maturities will have less spread widening than those of longer maturities. Finally, this section provides for several exemptions from the spread shock, but does not specify Treasuries. Although few, if any, corporate presently own these instruments, it would be beneficial to specify this point for greater clarity, even if it does appear obvious. For example, taken to an extreme, an examiner could require that off-the-run Treasuries are widened relative to a curve created using on-the-run instruments.

NCUA should also integrate core deposit assumptions on overnight accounts into the credit spread test. Overnight deposits related to members' settlement activity and liquidity needs are relatively stable and measurable over time and should be incorporated as core deposits in the NEV tests.

### c. Cash Flow Mismatch Sensitivity Analysis with 50 Percent Slowdown in Prepayment Speeds.

This proposal requires a corporate to perform the 30 basis point spread shock described above in conjunction with a 50 percent reduction in prepayment speeds, ensuring that its NEV ratio does not fall below one percent and that it does not decline by more than 25 percent. We recommend that the spread shock be tailored to the sector, as well as the maturity of the instrument.

Although it is widely recognized that a mortgage related product demonstrates volatile prepayment rates that are highly correlated to the level of interest rates, other asset classes permissible by the proposed regulation do not.

**d. Liquidity Management**

The proposed rule will require a corporate to demonstrate accessibility to sources of internal and external liquidity and keep a sufficient amount of cash and cash equivalents on hand to support payment systems obligations. We believe the borrowing limits and the secured borrowing limits are excessive. We would recommend eliminating the 30-day limit for liquidity purpose borrowing so long as borrowing is matched by a corresponding asset of similar structure, and eliminating the requirement for non-liquidity purposes.

As an overall comment to the ALM requirements, Florida Commerce believes that the ALM requirements overall are too onerous and the limitations will limit the ability of the corporate to provide valuable services to natural person credit unions. We do not believe that the ALM requirements as proposed will allow a corporate to create an investment portfolio that will allow sufficient net interest income to meet the new retained earnings requirement of the rule.

**IV. <u>Credit Risk Management</u>**

**a. Issuer Concentration Limits**

The proposal limits an obligor to 25 percent of capital. We believe this limit is too restrictive in that there are not enough highly rated counterparties available to comply with this limit. This is restrictive not only in terms of bank counterparties for Fed Funds transactions, but also in terms of identifying adequate high quality ABS trusts. This restriction would cause one to question the assumptions and accuracy of the sample balance sheet and earnings model provided in the proposal. We recommend amending the 25% single obligor investment limitation and allow a larger limit of 200% of capital on money market transactions with a term of 90 days or less.

**b. Sector Concentration Limits**

The proposal restricts a corporate from having a concentration above those specified. Although the rule provides for exclusions for several investments, Fed Funds are not specifically excluded. We recommend that Fed Funds be specifically excluded from the single obligor limit. As the rule already contains obligor limits and corporates will likely be heavy users of the overnight Fed Funds market given the weighted average asset life restrictions, we believe this clarification is necessary.

## V. Corporate CUSOS

We acknowledge that NCUA is concerned that corporate CUSOs present a systemic risk for a variety of reasons and appreciate the NCUA's desire to exercise more oversight and control over these entities. We are generally supportive of this effort. However, there are many legitimate and valuable services offered by CUSOs that may be eliminated by the rule and the limited categories authorized provided by the rule. We recommend a mechanism either to grandfather in, or transition in existing services, pending formal approval. We also suggest that the NCUA provide some sort of criteria outlining the factors that will be considered when approving or denying a non-listed CUSO activity.

## VI. Legacy Assets/Capital Replenishment

Florida Commerce has concerns over the proposed rule that requires a permanent depletion of capital and believes that corporates should be permitted to restore capital to its members if actual losses prove to be less than projected. GAAP does not require the extinguishment of capital based on estimated losses. CUNA and other organizations have proposed mechanisms that would allow for capital to be replenished. We support these concepts and hope the NCUA will consider allowing some method in this regard.

We further believe there needs to be a separation of legacy assets from new capital. Isolation of those assets will assist in the recapitalization of the corporate. Although the NCUA has indicated it is working on a solution in this area, we believe it needs to be included as part of this proposal so that the entire package of rules can be evaluated simultaneously.

## VII. PCA

We believe there needs to be some kind of phase in/transition period for PCA. With the newly imposed retained earnings minimums, capitalization requirements, and required leverage ratios, it is difficult to see how any corporate can comply in such short order. We believe a phased-in approach allowing the corporate to recapitalize would be a more sensible approach.

Finally, we are uncertain if any changes are forthcoming to Rule 703. Although the NCUA has not indicated any intention at this point to make substantial changes in those rules, many of the comments herein may need to be modified should the NCUA move forward in Rule 703.

Florida Commerce appreciates the NCUA's willingness to allow for public input on this rule.

Sincerely,

Cecilia D. Homison

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Chief Executive Officer

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